

PROFITABILITY-LIQUIDITY TRADEOFF: THE EVIDENCE ON MALAYSIAN LISTED COMPANIES

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ABSTRACT

This study attempts to examine the determinant of companies' profitability in Malaysia. This study used the net operating income to measure profitability of company; current ratio and cash gap are used to measure liquidity and sales are used to measure the size of company. The sample of this study comprise of 166 companies listed on the Main Board of Bursa Malaysia covering period of 1998 to 2003. Overall, the regression models showed that the current ratio (CR) is consistently positive and significant with net operating income (NOI). However, the negatively significant relationship is found between profitability and liquidity as measures by cash gap (cash conversion cycle). This study finds that CR is the most important liquidity measure that affects profitability. This study has observed the relationship between size and profitability of company. Size is also found to bear some influence over profitability. Therefore, the regression model showed that Malaysian companies have a positive relationship between NOI and size. Finally, this study suggests that size, current ratio and cash gap are significant determinants of the variability of profitability.

ABSTRAK

Kajian ini bertujuan untuk mengenalpasti penentu keuntungan bagi syarikat-syarikat di Malaysia. Kajian ini menggunakan pendapatan operasi bersih untuk mengukur keuntungan syarikat, nisbah semasa dan kekangan tunai digunakan untuk mengukur kecairan, dan jualan untuk mengukur saiz sesebuah syarikat. Sampel kajian ini merangkumi 166 syarikat yang disenaraikan, di Papan Utama Bursa Malaysia bagi tahun 1998 sehingga 2003. Keseluruhan model regresi menunjukkan bahawa nisbah semasa mempunyai hubungan positif yang konsisten dan signifikan dengan pendapatan operasi bersih. Bagaimana pun, hubungan negatif ditunjukkan antara keuntungan dan kecairan apabila kekangan tunai digunakan bagi mengukur kecairan syarikat. Kajian ini mendapati bahawa, nisbah semasa adalah ukuran kecairan yang lebih penting dan memberi kesan kepada keuntungan syarikat. Kajian ini juga melihat kepada hubungan antara saiz dan keuntungan syarikat. Saiz juga mempengaruhi keuntungan. Model regresi menunjukkan syarikat-syarikat di Malaysia mempunyai hubungan positif di antara pendapatan operasi bersih dan saiz. Akhirnya, kajian ini menunjukkan bahawa saiz, nisbah semasa dan kekangan tunai mempengaruhi kepelbagaian dalam keuntungan syarikat secara signifikan.

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LIST OF ABBREVIATION

CCC	:	Cash Conversion Cycle
CG	:	Cash Gap
CGS	:	Cash Gap in Days/ 100
CR	:	Current Ratio
LOGS	:	Logarithm of Sales
LOGTA	:	Logarithm of Total Asset
NOI	:	Net Operating Income
QR	:	Quick Ratio

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CHAPTER 1

INTRODUCTION

1.0 Chapter Overview

This chapter consists of 5 major areas i) introduction of the company's profitability and liquidity, ii) context of the research problem, iii) research objectives, iv) justification of the research, v) research scope, assumptions, limitations and vi) layout of the remaining chapter.

1.1 Introduction of the Company's Profitability and Liquidity

The term of working capital refers to the difference between resources in cash or already convertible into cash (current assets) and organizational commitments for which cash will soon required (current liabilities). The objective of the working capital management is to maintain the optimum balance of each of the working capital components. This includes the funds that are held as cash in bank such as fixed deposits. However, such cash are more appropriately be 'invested' in other assets.

The working capital management enhances a company's need in maintaining their liquidity as it affects the performance of company. It received the major portion of

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